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THE
WASHINGTON STREET SUBWAY

COMMENTS

ON THE

Financial Condition of the Boston Elevated Railway Co.

SUBMITTED BY

LOUIS D. BRANDEIS

ON BEHALF OF THE

BOSTON ASSOCIATED BOARD OF TRADE

TO THE

COMMITTEE ON METROPOLITAN AFFAIRS

OF THE

MASSACHUSETTS LEGISLATURE.

APRIL 26, 1902

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TO THE COMMITTEE ON METROPOLITAN AFFAIRS :

**Hearing of
April 14** On April 14, 1902, Mr. Pillsbury addressed your Committee in opposition to the Washington Street Subway Bill, originally introduced at the request of the Boston Associated Board of Trade and the Public Franchise League, and which (in a slightly amended form) has been adopted by Mayor Collins as expressing the wishes of the people of Boston and is urged by him for immediate passage.

**Purported
Disclosure** Mr. Pillsbury purported to state "frankly and fully" the financial condition of the Boston Elevated Railway Company, and asserted that this condition afforded a conclusive reason why "the burden" of a new subway should not be assumed by it.

**Multum
in Parvo** In the few minutes then remaining for reply, I stated to your Committee reasons why we believe that the Company can afford to take the new subway on the terms proposed by our bill; that it will gladly do so if it finds that the Legislature will not grant even better terms; and that the opposition of the Boston Elevated Railway Company is based really on the desire to secure permanent franchises.

**Analysis
in Detail** I now submit in more detail some of the facts relating to the financial condition of the Company upon which our conclusions are based.

Net Earnings Not Decreasing

FIRST. Mr. Pillsbury says—referring to the operation of the system by the Elevated Railway Company during the four years from September 30, 1897, to September 30, 1901,—“Net earnings are increasing in but half the ratio of gross earnings.”

This statement is incorrect.

Almost Four Per Cent According to the Company's reports net earnings are increasing in a greater ratio than gross earnings, for the percentage of operating expenses to gross earnings has decreased materially during that period, namely :

	Operating Expenses: Per Cent. of Gross Earnings						
1898	71.53
1899	70.59
1900	67.23
1901	67.97

More Than \$800,000 And net earnings from operation during those years have increased as follows :

1898 .. .. .	..	..	..	..	..	\$2,612,512.19
1899 .. .. .	..	..	..	..	..	2,844,290.37
1900 .. .. .	..	..	..	..	..	3,313,099.44
1901 .. .. .	..	..	..	..	..	3,456,395.78

West End Surpassed As compared with the last two years of the operation of the System by the West End Street Railway Company the decrease in the cost of the operation is even more marked :

	Operating Expenses: Per Cent. of Gross Earnings						
1896	75.93
1897	71.26

The actual net earnings from operation in those years having been as follows :

1896 .. .. .	..	..	..	..	..	\$2,007,339.15
1897 .. .. .	..	..	..	..	..	2,505,323.22

By Almost a Million These figures show that during the four years (ending September 30, 1901,) since the lease of the West End Street Railway system by the Boston Elevated Company, the gross earnings from operation increased \$2,073,961.31 or 23.78%, while the net earnings from operation increased \$951,072.56 or 37.96%.

The Fact About Fixed Charges

Half of a Truth **SECOND.** Mr. Pillsbury says that there has been "an increase in fixed charges in the four years of Elevated operations of \$748,034, or 84.9% exclusive of West End dividends."

This statement is at least misleading.

Chief Item Aside from Subway rental (which the West End had assumed before its lease to the Elevated) and the increase in the taxes (due mainly to the great rise in market values of West End and Elevated stock) the entire increase in fixed charges was \$87,950.67, which represents interest on money borrowed by the West End Company under direction of the Elevated Company to pay for 88 miles of additional surface track—the total track for surface cars operated by the Elevated Company having increased from 304 miles on September 30, 1897, to 392 miles, September 30, 1901.

Sine Qua Non Without the increased facilities afforded by the existing subway and the increased mileage the great increase in gross earnings from operation would have been impossible. For the two years prior to the lease to the Boston Elevated, the gross earnings from operation of the West End and the number of revenue passengers carried were as follows:

	Gross Earnings	Revenue Passengers
1896	\$8,341,958.29	166,862,288
1897	8,719,031.78	172,554,513

\$500,000 and Ten Million Passengers For the four years after the lease to the Boston Elevated the gross earnings from operation and revenue passengers carried were as follows:

	Gross Earnings	Revenue Passengers
1898	\$9,179,096.35	181,321,295
1899	9,671,440.67	191,023,224
1900	10,141,209.68	201,124,710
1901	10,792,993.09	213,703,983

In other words: The gross earnings in the
Elevated Far four years, September 30, 1897, to Septem-
from a Burden ber 30, 1901, increased \$2,073,961.31

The net earnings from operation increased \$951,072.56
(all from the surface lines except during the short period
from June 10 to September 30, 1901).

And the total increase of fixed charges, other than or-
dinary taxes, was :

Increase in interest	\$ 87,950.67
Increase in net Subway rental, about ..	189,541.33
Compensation tax	94,438.69
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	\$371,930.69

Increase of net earnings over increase
in charges other than ordinary taxes, \$577,183.20

This alone was sufficient to pay the 5¾% dividend on
the \$10,000,000 Elevated Company stock.

Great Saving On the other hand, Mr. Pillsbury does not
at Hand disclose to the Committee the reduction in fixed
charges about to begin by which one-half of all
outstanding bonds will be refunded at a low rate of interest,
say 3.75%, which will effect a reduction in the fixed charges
of about \$65,500.

The following bonds are about to mature:—

Highland Street Rwy. Co., 5%, due May, '02,	\$ 300,000
West End " " 5%, " Nov., '02,	3,000,000
Cambridge " " 5%, " Apr., '03,	390,000
Metropolitan " " 5%, " Dec., '03,	500,000
Charles River " " 5%, " Apr., '04.	150,000
Middlesex " " 5%, " July, '04,	200,000
South Boston " " 5%, " May, '05,	200,000
Boston Cons. " " 5%, " June, '07,	500,000
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	\$5,240,000

The annual saving, refunding these on the basis of say
3.75%, will be \$65,500. It thus appears that when these

refunding operations are completed the net increase of interest charge, in spite of 88 miles of new surface tracks, will be only \$22,450.67.

Concerning Increased Taxes

THIRD. Mr. Pillsbury says: "The percentage of taxation to investment in 1897 was 1.5. In 1901 it was 2.3. While the investment is rapidly increasing especially with the construction of the elevated road, taxation is increasing in nearly two and one-half times the ratio of investment."

This statement is misleading.

The rate of taxation has not increased appreciably since 1897. The increase of taxes is due to the increase in the market value of the stock taxed. That increase in market value is due largely to the special privileges granted by the State to the Elevated Railway by the act passed June 10, 1897.

	Mar. val. pr. sh. May 1, '97.	Mar. val. total cap. May 1, '97.	Mar. val. pr. sh. May 1, '01.	Mar. val. total cap. May 1, '01.
West End pfd.,	\$ 94	\$12,032,000	\$117.00	\$14,976,000
West End, com.	72	13,082,400	98.50	17,897,450
Boston Elevated, (1898 to 1900) issued at	105	10,500,000	177.00	17,700,000
		<u>\$35,614,400</u>		<u>\$50,573,450</u>

On a Gift of
\$5,000,000

The effect of the Act of 1897 (as the opponents of that bill predicted) was to make a present to the West End stockholders of franchises shown to be worth, by the rapid rise in the stock, fully \$5,000,000. The additional taxes paid since 1897 are merely taxes on the gift then made by the State at the request of the Boston Elevated Railway Company. The taxes paid by the Company on the market value of all stock relieve the stockholders from the payment of any taxes and make the dividend re-

ceived a net income. The market value is high not only because the dividend is high, but also because the stock is exempt from taxes.

Increase at an End The rate of dividend on the West End stock being limited since the lease to the Elevated Company, there has been no further appreciable rise in the market value of the West End stock or increase in the taxes paid on account of that stock.

Tax paid on West End stock and property :

1899	..	..	..	..	..	\$500,575.24
1900	..	..	..	..	..	504,748.45
1901	..	..	..	..	..	513,207.91

and further appreciable increase is not to be expected.

Cui Bono Mr. Pillsbury says: "We are paying more to the public today in taxes than we are paying to our stockholders in dividends by the sum of \$320,000 per annum." The dividend is stated at "5¾%, \$575,000. Taxes in 1901, \$895,065." The comparison is misleading. The taxes given are the total on the whole system, West End and Elevated; the dividends given are only the dividends on the Elevated stock. But the dividend on the West End stock is \$1,147,950. So that if the total tax is \$895,067, the total paid in dividends is \$1,722,950, a sum not \$320,000 less, but \$827,883 more than the tax.

Ratio of Permanent Investment to Net Earnings

FOURTH. Mr. Pillsbury says: "In the last four years we have added nearly \$17,000,000 to the permanent investment, which has increased in more than four and a half times the ratio of net earnings, so that while in 1897 the net income of the investment was 8.4% it is now but 6.1%."

This statement is grossly misleading.

Discrepancy of Nearly \$3,000,000

(A) The balance sheet of September 30, 1901, shows but \$14,316.08 increase in invested capital. The only new capital invested in the West

End-Boston Elevated System from September 30, 1897, to September 30, 1901, is the following :

(1) The amount raised by the issue of West End Street Railway Company debentures sold on a basis of about $3\frac{3}{4}\%$ and used to pay for the eighty-eight miles of extension of surface lines.

(2) \$10,500,000 raised by the sale of Boston Elevated Railway Company stock to construct the Elevated railroad.

The additional cost of the Elevated Railway up to September 30, 1901, alleged to be about \$2,500,000, seems to have been paid for since September 30, 1901, not from new capital invested, but in part from money borrowed temporarily on the market at a low rate of interest, and in part from funds earned by the Boston Elevated Railway Company during the four years between September 30, 1897, and September 30, 1901, and set apart (in addition to the dividends paid) as special funds, namely :

Damage Fund	\$425,262.48
Insurance Fund	300,000.00
Depreciation Fund	600,000.00
Surplus Fund	663,509.07
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	\$1,786,771.55

(B) The principal answer, however, to the statement of Mr. Pillsbury is this :

The earnings made by reason of seven miles of Elevated lines which he says cost them \$12,500,000, are not represented, except to a slight extent, in the earnings of the years ending September 30, 1901. No part of the Elevated lines was opened until June 10, 1901. The Atlantic Avenue line was not opened until August 22, 1901. The full earning capacity of these lines is even now impaired by reason of insufficient cars, the fifty additional cars required and ordered, as Mr. Pillsbury states, not having arrived. Some idea may

however be formed from data at hand of the probable increase by reason of the Elevated lines when fully equipped: President Bancroft says in the report to the stockholders for the year ending September 30, 1901, "The increase in traffic revenue during the months in which the Elevated road was in operation as compared with the increase in the corresponding months of the previous years was 8.57% as against 3.54%.

Revenue Increased In other words, an extra increase of traffic of over 5% was made during the whole period from June 10, 1901 to September 30, 1901, although part of the Elevated lines was not opened until August 22, 1901 and none of it was adequately equipped. This extra 5% increase of revenue passengers, continued throughout the year at the same operating cost would yield about \$352,125.32 additional gross earnings and \$112,680.10 net earnings, if the percentage of operating expenses remained the same.

An Absurd Comparison To point to last year's income as showing what the system earns is as misleading as if a real estate owner who had expended \$12,500,000 on additional buildings which were not completed until three months before the end of the year and even then were not fully occupied took the year's net income as a test of the net earning capacity of the whole property.

Elevated System a Benevolent Enterprise?

FIFTH. Mr. Pillsbury says: "The truth is that the whole Elevated system was created and exists more for the relief of travel than any addition to profits of the system, for passengers who take the Elevated trains do not at the same time take surface cars."

Capitalization of West End Profits (a) It must be a surprise to the community to learn that the Boston Elevated Railway Company was "created" by the New York and Boston bankers, as an eleemosynary institution, and not for the purpose of capitalizing the immense profits of

the West End System. (The surplus in 1897 over all dividends was \$431,572.66.)

Development at a Standstill (b) It certainly is not true that "the Elevated lines" do not exist now for the "profit of the system." The fact is that while the building of the Elevated lines was compulsory under the Act of 1897, it was necessary also in order to maintain the increase in earnings for the Company to have these Elevated lines, just as the existing subway had become necessary in 1897, and the new Washington Street Subway will be as imperatively necessary by the time it can be completed.

The increase in revenue passengers on the West End lines in 1896 over 1895 had been 11,630,782. The increase in gross earnings was \$595,787.52. The increase in revenue passengers of 1897 over 1896 was only 5,692,225 and the increase in gross earnings only \$377,073.49.

The reason for the diminished rate of growth was that the carrying capacity of the road in the heart of the city had been practically reached.

In the fall of 1897, after the subway was opened, the large increase in revenue passengers carried and in gross earnings was resumed.

		Revenue Passenger Increase	Gross Earnings Increase
1898	.. 5.08%	\$ 8,766,782	\$460,064.57
1899	.. 5.33%	9,701,929	492,344.32
1900	.. 5.28%	10,101,486	469,769.01

History Repeats Itself In 1901 before the opening of the Elevated lines, the carrying capacity in the heart of the city had again been practically reached so that the increase in the revenue passengers and gross earnings of the System for the eight months and ten days up to June 10, 1901, (when the first Elevated lines were opened) was only 3.54% as against an average of 4.47% during the three preceding years. Upon the opening of the Elevated lines the increase jumped to 8.57%, and when fully equipped the increase will doubtless be larger.

**Self Interest
Requires a
New Subway**

But full equipment of the Elevated lines will not suffice unless they can be run to the best advantage, and it is obvious that the Elevated lines cannot be so run except through the Washington Street subway. The Elevated Company needs the new subway for its added carrying capacity and for its greater economy, just as in 1897 the existing subway, and in 1901 the Elevated lines had become necessary for its continued prosperity.

No New Obligations Before 1905

SIXTH. Mr. Pillsbury says: "Our earnings must be allowed to overtake our obligations."

**A Margin
for Profit**

It must be remembered that the rental of the new subway will not be payable until the subway is built, that is, not before October, 1905. Meanwhile substantially no new obligations will be assumed by the Elevated Company.

**Lesson of
Experience**

On the other hand, net earnings from operations owing to growing traffic will be steadily increasing. An increase of gross earnings for the three years even at so low a rate as five per cent, would yield \$1,701,245.62, and at the present operating cost, \$544,398.60 *additional net earnings* before any new subway rental becomes payable. As soon as the new subway is opened largely increased traffic and earnings must result according to uniform experience.

The Rate of Rental

Stultification

SEVENTH. Mr. Pillsbury says that the bill advocated by Mayor Collins, the Board of Trade and others cannot be accepted, because in requiring a rental of 4 $\frac{7}{8}$ % of cost it imposes too great a burden on the Elevated Company. The action of the Elevated Company last year shows conclusively that such is not the opinion of the Company.

**Inconsistent
with Attitude
of Last Year**

At the last session of the Legislature the Elevated Company endeavored to have a bill passed by which it should pay the whole cost of the new Washington Street Subway to be owned by the City, but leased to the Elevated Company free for forty years. The cost was estimated at \$6,000,000, and the construction of the subway under that bill would have placed upon the Company an annual charge of at least $4\frac{7}{8}\%$ of its cost, for the Company could not borrow at as low a rate of interest as the City.

**The Struggle
For
Permanency**

Still the Company made every effort to secure the passage of that bill, and to defeat the Board of Trade bill, although under it the City was to pay the cost and lease the subway to the Elevated Company at a rental of $4\frac{7}{8}\%$. The real objection of the Elevated Company to the Board of Trade Bill was not that it imposed too great an immediate annual charge, but that it granted a lease for only 20 years; whereas the purpose of the Elevated Company throughout has been to secure a franchise for a long term of years in the hope of its resulting ultimately in a permanent franchise.

**Relation of
Rent Charge to
Sinking Fund**

It is urged that the rental should be less than the $4\frac{7}{8}\%$ which was fixed in 1896 for the rental of the existing subway because the rate of interest has fallen since 1896, and the City can borrow cheaper now than it could then. Confessedly, the rental must be large enough to meet not merely the annual interest, but also the annual sinking fund charge. The amount of the annual sinking fund charge must be sufficient when re-invested at the then current rate of interest, to yield at least enough to pay the bonds at maturity. As the rate of interest is falling, a larger sinking fund charge becomes necessary. Hence a decline in the rate of interest does not materially reduce the amount of rental necessary, because a larger sinking fund charge is required.

Those Elevated Locations EIGHTH. Mr. Pillsbury says: "Our tenure of our elevated locations is permanent. If we create the tunnel, a substituted and better elevated location [through the city for the Elevated road] there is no reason why our tenure of that should not also be permanent." "We now have two such locations upon which the demands of traffic might drive us to build if we cannot do better."

Meig's Road Mr. Pillsbury doubtless refers to the following locations originally granted to the Meigs road by the Act of 1894, c. 548.

"To and through Beverly street, to and through Haymarket Square, to and through Union street, to and through Dock Square, to and through a new street which shall be built by said city, of the width of eighty feet, and one half of the cost of which shall be paid by said corporation, in the line of Congress street, between State street and Dock Square, to and through Congress street and Post Office Square, to and through Federal street, to and over Federal street bridge." . . .

"To and through Cambridge street, to and over Craigie bridge or a new bridge across Charles river to a point on Charles street, between Allen and Poplar streets in Boston, through Charles street, to and through Leverett street, to and through Brighton Street, to and through Lowell street, to and through Causeway street, to and through Portland street, to and through Merrimac street, to and through Washington street, to and through Dock square, to and through Devonshire street, to and through Franklin street, to and through Arch street, to and through Chauncy street, to and through Harrison avenue, to and through Kneeland street, to and through Washington street to its junction with Hyde Park avenue."

To and Through Think of the Elevated Company building on either of these locations. The land damages would be greater than the whole Elevated stock even at the present high value. Such locations are about as valuable as locations to and through the moon. Think of the Elevated Company being 'driven to build' on such loca-

tions when the City offers to let the Elevated Company have the subway at a rental of not more than it would cost the Elevated as an annual charge if it built and owned the subway itself.

* * * * *

Board of Trade Bill.

Endorsed by
Opinion and
Precedent

No reason has been shown, no reason can be shown, why the bill introduced by the Associated Board of Trade and the Public Franchise League should not become a law. It rests upon the solid foundation of past experience, for it is but an extension to Washington Street of the existing Subway System. It embodies the fundamental principles of public ownership and control by short lease which Governor Crane has made the recognized policy of the Commonwealth. It is adopted and urged for immediate passage by Mayor Collins as expressing the wishes of the people of Boston. It is supported by the trade and the labor organizations and an almost unanimous public opinion. Its provisions are simple: Construction by the Transit Commission at the expense of the City, the subway to be its property forever; lease to the Elevated Company for 25 years from the date of the Act at a rental of $4\frac{7}{8}\%$ of the cost, and if accepted the lease of the existing subway to be extended so as to expire at the same time (1927);—Rights to lease to some other company if the Elevated does not take the lease. Referendum to the people of Boston.

The bill protects the public; it is fair to the Elevated Company; it should be enacted.

The Struggle for Protection.

Fruits of
Vigilance

As Mr. Pillsbury has been unable to discover a single feature of the Board of Trade bill (except the amount of the rental) to which even he could address any specific criticism, he has occupied himself with vehemently asserting that the men who advocated it are impractical and ignorant. It may be proper to recall

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some of the practical results which these men have aided in accomplishing in the attempts which have been made to protect the public from the aggression of the railway companies.

1896. Term of the possible subway lease, reduced from fifty years to twenty years. Acts of 1896, Chap. 492.

1896. Car toll provision inserted in lease of subway to West End Company. (Transit Commissioners and Railroad Commissioners.)

1897. Provision for compulsory building of seven miles elevated lines inserted in bill, and free transfer provisions extended. Acts of 1897, Chap. 500.

1897. Length of lease of West End system to Elevated Company reduced from 99 years to less than 25 years. Rental reduced about \$100,000 by reducing dividend on West End common stock from 8% to 7%.

1899. Referendum added to Elevated Company bill to prevent taking up tracks on Tremont Street, and bill rejected at the polls. Acts of 1898, Chap. 390.

1900. So-called Citizens' Association-Elevated Company bill defeated. The bill provided that the Elevated Company should construct at its own expense, and own in perpetuity the Washington street and Cambridge street subways, subject to the right of Boston to buy them at cost after 1937, if it so voted sometime between 1937 to 1940. It also provided that the lease of the existing subway should be extended to 1937.

1901. The Elevated Railway Company's Washington Street Subway Bill defeated. That bill provided for the construction at the expense of the Elevated Company and ownership by the City, but was vetoed by Governor Crane mainly because it gave the Elevated Company a forty-year lease.

The public interests have been protected, transportation facilities have been increased, and Elevated Company Stock has, nevertheless, risen from 105 to 170.

BOSTON, April 26, 1901.

LOUIS D. BRANDEIS.

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